

Motor Vehicle Fuel Tax Law  
(Title 18, Division 2, Chapter 1 of the California Code of Regulations)  
Adopt regulations 1123, 1124, 1161 and 1178;  
Amend regulations 1101, 1105, 1120, 1132, and 1134; and  
Repeal regulations 1103, 1104, 1106, 1107, 1108, 1114, 1115, 1116, 1117, 1118, 1110, 1121,  
1131, 1133, 1151, 1152, 1153, 1154, 1155, 1171, 1172, 1173, 1174, 1175, and 1176:  
and  
Diesel Fuel Tax Law  
(Title 18, Division 2, Chapter 3 of the California Code of Regulations)  
Adopt regulations 1435 and 1436;  
Amend regulations 1420, 1422, and 1430.

INITIAL STATEMENT OF REASONS  
PLAIN ENGLISH OVERVIEW  
NON-CONTROLLING SUMMARY

Regulation 1101 Defines Motor Vehicle Fuel.

Existing Regulation 1101 is proposed to be amended to reflect changes in the definition of motor vehicle fuel under the Motor Vehicle Fuel Tax Law that took effect on January 1, 2002. The new definition of motor vehicle fuel is found in part in several sections of the Revenue and Taxation Code. The proposed regulation places the various components of the definition in one place. Also, the proposed regulation identifies what is not motor vehicle fuel. For example, the law identifies gasoline blendstocks as a petroleum product component of gasoline and includes them in the definition of motor vehicle fuel. The proposed regulation at 1101(f)(1) lists the products that are gasoline blendstocks and, like the Internal Revenue Service Regulation 48.4081-1, at 1101(f)(2) clarifies what is not a gasoline blendstock.

Under the proposed regulation, "racing fuel" is excluded from the definitions of motor vehicle fuel at 1101(a) and blended motor vehicle fuel at 1101(g). Industry representatives suggested that the racing fuel definition in 1101(h) be divided into leaded racing fuel and unleaded racing fuel. Leaded racing fuel is defined in subdivision (h)(1) to mean fuel that (i) generally is used in vehicles not eligible to be registered for highway use, and (ii) is not diesel fuel, kerosene or gasoline blendstock, and (iii) has an octane rating of 100 or higher, and (iv) contains 1.0 gram of lead per gallon or more, and (v) does not meet the ASTM specification for gasoline. Unleaded racing fuel is defined in subdivision (h)(2) to mean fuel that (i) is not diesel fuel, kerosene or gasoline blendstock, and (ii) has an octane rating of 100 or higher, and (iii) does not meet California Air Resources Board specification for gasoline.

Regulation 1105 Defines Tax-Paid Fuel and Ex-Tax Fuel.

Existing regulation 1105(a) defines "tax-paid fuel" and "ex-tax fuel" and existing regulation 1105(b) provides that a distributor or broker who acquires tax-paid fuel from a licensed motor vehicle fuel distributor or broker is not liable for tax on the tax-paid gallons, that a distributor who fails to invoice or collect tax on a taxable distribution remains liable for the tax, and that a distributor who distributes ex-tax fuel to a qualified distributor and indicates that the fuel is tax-paid remains liable for tax on that fuel.

Under the Motor Vehicle Fuel Tax Law that took effect on January 1, 2002, tax is imposed on a supplier upon removal, entry, or sale of motor vehicle fuel instead of on the distribution by a distributor or broker. Therefore, on and after January 1, 2002, it is no longer necessary to explain the continuing tax liability of a distributor upon distribution of fuel. For that reason, the existing 1105(b) is proposed to be repealed. The terms "tax-paid fuel" and "ex-tax fuel" are proposed to be defined at 1105(a) and 1105(b) respectively and other minor clarifying changes are proposed to be made to those definitions. In addition, at 1105(a)(2) a purchase receipt which shows that tax was included in the amount a purchaser paid for the motor vehicle fuel is listed as the type of documentation which supports a claim that fuel is tax-paid. The proposed regulation is nearly identical to existing Board Regulation 1413, which pertains to the Diesel Fuel Tax Law.

#### Regulations 1120 and 1436, Returned Sales and Invoice Corrections.

Statutory changes effective January 1, 2002, necessitated that Regulation 1120 be amended in subdivision (a) to refer to a supplier instead of a distributor and to clarify how a supplier is to handle motor vehicle fuel returned by a customer. The regulation explains that when motor vehicle fuel is returned to a refinery or an approved terminal by the supplier, the supplier may either file a claim for refund with the State Controller or take a credit on the supplier's tax return. The regulation presumes (i) that the supplier purchased the motor vehicle fuel tax-paid if the credit memorandum includes motor vehicle fuel tax and (ii) that for purposes of a refund or credit, the supplier subsequently removed the motor vehicle fuel from a terminal rack in the same month that the motor vehicle fuel was returned.

In response to industry comments, "refinery" has been added in (a)(1) and (a)(3)(A) to reflect the fact that the fuel may be returned to both an approved terminal or to a refinery. The credit will be allowed on the supplier's tax return only if the following conditions are met: (i) the returned fuel is delivered into a refinery or an approved terminal, (ii) the credit is taken on a tax return filed within three months after the close of the calendar month in which the motor vehicle is returned, (iii) the supplier prepares a First Taxpayer's Report on the returned fuel, and (iv) a copy of the First Taxpayer's Report and credit memorandum are retained for inspection by the Board with the tax return.

Also, in response to industry comments, the proposed regulation adds the word "only" to (a)(3)(D) clarifying that when a tax return is filed electronically, only a copy of the First Taxpayer's Report and credit memorandum are to be mailed as opposed to the complete return. A similar request for clarification was also made as to (b)(3), however, it has been decided that subdivision (b) should be deleted an unnecessary recordkeeping requirement that is covered adequately in proposed Regulation 1178.

In addition, the industry proposed that the conditions to allow a credit on a tax return at (a)(3) be changed to allow, in addition to the First Taxpayer's Report and credit memorandum, "other similar documentation that may be a statement from the seller". The Board staff has not included that change because it believes the minimum documentation required to support the credit is the First Taxpayer's Report and credit memorandum. It would not be prudent to rely on a "statement from the seller" as the basis for allowing a credit for taxes on a return for several reasons, including the fact that requested change does not require that the statement be contemporaneous with the sale. Also, the industry suggested language that the documentation "must be retained by the supplier for audit purposes". The Board staff would substitute instead that the documentation must be retained for "inspection by the Board", so that the information would be available for purposes other than audit, such as verifying the claim for refund or credit.

If a supplier fails to claim a credit in the specified manner, it may only file a claim for refund with the State Controller to recover the tax. The regulation lists the information and documentation that is required to be included in the claim for refund. Also, the claim must be filed within three years from the date of return of the fuel.

Industry suggested that the time for filing a claim for refund for tax paid twice on returned fuel should not refer to the second tax, but rather should tie into the time when the credit is allowed to be taken on a return. In response to that comment, the refund claim filing provision at (a)(4)(C) was changed to refer to the "date on which the claimant received the returned fuel" instead of the "date on which the claimant incurred liability for the second tax." Proposed Regulation 1120 subdivisions (a)(4)(D) and (a)(4)(E) were removed from the regulation as unnecessary in light of the other changes made.

Subdivision (b), which deals with invoice correction, is repealed because the record keeping requirements are covered in Regulation 1178, Records. The repeal of the subdivision (b) takes care of the industry concerns about the way business is currently conducted.

The diesel fuel Regulation 1436 is a new regulation, which provides that when diesel fuel is returned to the supplier by a customer and delivered into a refinery or an approved terminal, the supplier may either file a claim for refund of the tax with the Board or take a credit on the supplier's tax return. The regulation explains when and how the credit may be taken and when a refund must be filed. The regulation is identical to Regulation 1120 except that the regulation explains that the claim for refund of the diesel fuel tax must be filed with the Board, rather than with the State Controller.

The same changes which were made to Regulation 1120 in response to comments from the industry have been made to regulation 1436.

Regulations 1123 and 1420, Supplier.

Effective January 1, 2002, Section 7338 of the Revenue and Taxation Code defined the term "supplier" to include blenders, enterers, position holders, refiners, terminal operators, and

throughputters. The proposed regulation identifies the various types of motor vehicle fuel suppliers and describes the imposition of the motor vehicle fuel tax and the reporting requirements of each. The proposed regulation also describes the circumstances in which the terminal operator is jointly liable with a supplier for the removal of motor vehicle fuel from the terminal rack. The proposed regulation is nearly identical to the Board's existing Diesel Fuel Tax Regulation 1420.

The following industry suggestions were included in the regulations:

- (1) Since a supplier files only one tax return, the following sentence should be dropped "A supplier acting in more than one capacity ... may be required to file more than one return or report." The sentence was dropped for (a).
- (2) A refiner removes fuel from a terminal rack located at a refinery instead of a refinery rack. (b)(4)(A) was rewritten to refer to a terminal rack located at a refinery instead of to a refinery rack.

Industry had a concern that subdivision (B) of (b)(4) did not include fuel sold to unlicensed suppliers after the fuel leaves the refinery. Staff is reviewing this concern and the application of subdivision (c) of Section 7363 of the Revenue and Taxation Code to the regulation. Subdivision (c) imposes tax on "the removal or sale of motor vehicle fuel in this state to an unlicensed person unless there was a prior taxable removal, entry, or sale of the motor vehicle fuel."

The existing Diesel Fuel Tax Regulation 1420 is being revised in accordance with the industry suggestions noted above. Also, Section 60203 that requires a throughputter to file a separate tax return was repealed effective January 1, 2002. For that reason, the last sentence in (a) is being dropped since it refers to a separate throughputter return.

#### Regulations 1124 and 1422, Relief From Liability.

Effective January 1, the Motor Vehicle Fuel Tax Law, Section 7657.1, of the Revenue and Taxation Code, provided that a taxpayer may be relieved of liability from the Motor Vehicle Fuel Tax, including penalty and interest, if the Board finds that the person's failure to make a timely return or payment was due to the person's reasonable reliance on written advice from the Board. Regulation 1124 is proposed to clarify the circumstances under which relief may be granted for reliance on written advice of the Board. The proposed regulation is nearly identical to the Board Regulation 1705, which pertains to the Sales and Use Tax Law.

Existing Diesel Fuel Tax Law Regulation 1422 is being revised to conform to Sales and Use Tax Regulation 1705 and to proposed motor Vehicle Fuel Tax Regulation 1122. The proposed changes include written advice in the form of an annotation or legal ruling of counsel under the conditions set forth in new subdivision (d). Also, new subdivision (e) adds that a trade or industry association requesting advice for its members must identify the member for whom the advice is requested in order for the relief from liability to apply. These revisions make Regulation 1422 nearly identical to the other Board regulations on relief from liability.

### Discussion of Regulations 1132 and 1430, Shipments Out of the State.

As a result of the statutory changes that became effective January 1, 2002, this regulation is proposed to be amended to replace references to "distributor" with references to "supplier". The existing regulation provides that stock transfers of ex-tax fuel to a point outside California are not distributions and therefore are not subject to tax. With the changes in point of imposition of tax that took effect January 1, 2002, this instruction is no longer relevant. Therefore the language pertaining to stock transfers is proposed to be deleted from subdivisions (c) and (d).

In addition, in subdivision (d), the time for taking a credit on a tax return was proposed to be changed from "within three months after the close of the calendar month in which the tax-paid fuel is exported" to a requirement that "the credit be claimed on the return filed for the month in which tax-paid fuel was exported." In the interested parties meeting held on August 9, 2001, both industry and the State Controller's office objected to the change. Therefore, the time for taking the credit will remain within three months of the month of export. This will not increase the number of refunds filed with the State Controller.

The proposed regulation is nearly identical to the existing Board Regulation 1430, which pertains to the Diesel Fuel Tax Law. Industry asked that Regulation 1430 be amended to allow the credit in (b)(2) to be claimed on a return filed within three months after the close of the calendar month in which the tax-paid fuel is exported. This will make the time for taking a credit or filing a claim for refund the same in both Regulation 1430 and Regulation 1132. Regulation 1430 is proposed to be amended for this change.

Industry had a concern about the requirement that exports be supported by a written contract that requires the supplier to deliver fuel out of the state in order to qualify for exemption from tax. After reviewing the law, industry and staff agreed that a statutory change would be required to remove the requirement for an underlying written export contract.

### Discussion of Regulation 1134, Sales to the United States

The first two paragraphs of the existing regulation were designated as subdivision (a) and within that subdivision, references to "distribution" and "distributor" were replaced with "sales" and "seller" to conform to the definitions in the new law which became effective on January 1, 2002. Subdivision (b) was added to clarify that a supplier making a sale of ex-tax fuel to the United States armed forces may claim an exemption on the supplier's tax return. Subdivision (c) was added to clarify that any person making a sale of tax-paid fuel to the United States armed forces shall file a claim for refund of the tax with the State Controller.

The remainder of the existing regulation is proposed to be repealed as no longer necessary since Revenue and Taxation Code Sections 7401, 7486 and 7487 (relating to exemptions for distributors and brokers and to bond requirements of distributors and brokers) were repealed effective January 1, 2002.

Regulations 1161, Tax Paid Twice on Motor Vehicle Fuel, and 1435,  
Tax Paid Twice on Diesel Fuel

When a supplier is required to pay tax on the removal from a terminal rack of motor vehicle fuel on which a prior tax was paid, the supplier may either file a claim for refund of the tax with the State Controller or take a credit on the supplier's tax return. The regulation explains when and how the credit may be taken and when and how a refund claim must be filed. The regulation defines a first taxpayer as the person paying to the State the first tax on the fuel and defines a second taxpayer as the person paying to the State the second tax on the fuel.

The following industry suggestions are included in the regulations:

- (1) The tax paid twice credit should be taken on a tax return filed within three months after the close of the calendar month in which the second tax was reported to the state instead of the month when the second tax is reported. This suggestion was added to (b)(3) and (d) and will make all the credits in lieu of refund the same as in Regulations 1120 and 1436.
- (2) Instead of filing the First Taxpayer's Report with the tax return, the First Taxpayer's Report must be retained for inspection by the Board with the tax return on which the credit is claimed. This was added to (b)(5) and (c)(1). A credit may be taken on a supplier's tax return. The regulation explains that the second taxpayer must take the credit on a tax return filed within three months after the close of the calendar month in which the second taxpayer pays the second tax by reporting the gallons on its tax return. The first taxpayer must have paid the first tax by reporting the gallons on its tax return. Also, the first taxpayer must not have received a credit or refund of the first tax.

The regulation explains when a First Taxpayer's Report must be retained and to whom a copy of the report must be given. The regulation explains that when a person receives a First Taxpayer's Report and subsequently sells the fuel, the person must give a copy of the First Taxpayer's Report and a Statement of Subsequent Seller to the buyer. The regulation contains a model of the First Taxpayer's Report and the Statement of Subsequent Seller that outlines the information required. The model report and statement contain all the items of the Federal models plus some specific state items.

A claim for refund must be filed with the State Controller when the credit is not taken on a supplier's tax return filed within three months after the close of the calendar month in which the second tax gallons were reported. The regulation explains the information to be included in the claim for refund and that a copy of the First Taxpayer's Report and Statement of Subsequent Seller must be attached. Also, the claim must be filed within three years from the date of purchase of the fuel.

Regulation 1435 is proposed to be added regarding diesel fuel. When a supplier is required to pay tax on the removal from the terminal rack of diesel fuel on which a prior tax was paid, the supplier

may either file a claim for refund of the tax with the Board or take a credit on the supplier's tax return. Regulation 1435 explains when and how the credit may be taken and when a refund claim must be filed. The regulation is identical to Regulation 1161 except that the regulation explains that the claim for refund of the diesel fuel tax is to be filed with the Board.

#### Regulation 1178, Records

Effective January 1, 2002, the Motor Vehicle Fuel Tax Law, Sections 8253, 8301, 8302 and 8303, of the Revenue and Taxation Code, provided that a taxpayer must maintain and make available records and source documentation in such form as the Board may require. The proposed regulation specifies the records and documentation that are necessary and the form in which they should be maintained in order to support reported amounts. Since many businesses use automated data processing systems and reproductions from microfilm and microfiche, the proposed regulation stipulates the required form and content for automated records and reproductions from microfilm and microfiche. The proposed regulation informs taxpayers how long records must be retained and provides that records must be made available for the Board's examination during that time. Since failure to maintain and keep complete and accurate records may be considered evidence of negligence or intent to evade the tax, the proposed regulation informs taxpayers that such failure may result in penalties or other administrative action. The proposed regulation is nearly identical to the existing Board Regulation 1698, which pertains to the Sales and Use Tax Law.

#### Discussion of Motor Vehicle Fuel Tax Regulations to be Repealed

Effective January 1, 2002, Chapter 1053, Statutes of 2000, (AB 2114) changed the definitions, imposition of tax and exemptions in the Motor Vehicle Fuel Tax Law. Also, the sections of the Motor Vehicle Fuel Tax Law dealing with returns and records were repealed or amended. As a result of these statutory changes the twenty-five Motor Vehicle Fuel Tax regulations listed below are obsolete, and should be repealed:

- Regulation 1103, Blending or Compounding;
- Regulation 1104, Consignment for Sale;
- Regulation 1106, Tax-Paid Fuel Distributed;
- Regulation 1107, Drip Gasoline Producer;
- Regulation 1108, Qualified Distributor;
- Regulation 1114, Book Transfers, In-Tank Transfers, Physical Exchanges and Settlements;
- Regulation 1115, Pipeline Overages and Shortages;
- Regulation 1116, Losses Prior to Distribution;
- Regulation 1117, Allowable Losses of Commission Agents;
- Regulation 1118, Distribution of Commingled Fuel;
- Regulation 1119, Tax-Paid Motor Vehicle Fuel Blended, Compounded or Redistilled;
- Regulation 1121, Temperature Corrected Distributions;
- Regulation 1131, Natural Gasoline Sales to Licensed Distributors;
- Regulation 1133, Exempt Distributions to a Qualified Distributor;

Regulation 1151, Monthly Return of Distributor;  
Regulation 1152, Weekly Return of Distributor;  
Regulation 1153, Processor's Return of Distribution;  
Regulation 1154, Owner's Return of Processing Transactions;  
Regulation 1155, Recipient's Return of Processing Transactions;  
Regulation 1171, Distributor's Inventory and Stock Record;  
Regulation 1172, Producer's Stock Record;  
Regulation 1173, Producer's Purchase Record;  
Regulation 1174, Producer's Sales Record;  
Regulation 1175, Broker's Purchase Record; and  
Regulation 1176, Broker's Sales Record.

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